HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: HB 5201A PCB PECA 09A-01 Economic Development
SPONSOR(S): Economic Development & Community Affairs Policy Council; Murzin
TIED BILLS: **IDEN./SIM. BILLS:**

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR
Orig. Comm.: Economic Development & Community Affairs Policy Council	13 Y, 0 N	Kruse	Tinker
1) Full Appropriations Council on Education & Economic Development		Creamer	Martin
2)			
3)			
4)			
5)			

SUMMARY ANALYSIS

The bill addresses the charge to the Legislature in the Joint Proclamation issued December 30, 2008, to stimulate investment in the state's economy. The bill takes a two-pronged approach—creating a direct loan pilot program and a technical assistance for business pilot program—both utilizing Economic Gardening concepts. In the first prong, the bill creates a state-financed, business loan pilot program where qualified applicants may receive low-interest loans for up to a seven-year term contingent upon job creation goals being met. The second prong provides a technical assistance program to focus economic development efforts on growing existing businesses in the state that fall within the same parameters as those that would qualify for the loan program. Those parameters include businesses that:

1. are for-profit, privately held, investment grade;
2. employ between ten and 99 employees;
3. have been in existence in the state for at least two years;
4. generate between $1 million and $50 million in annual revenue;
5. qualify for the Qualified Target Industry (QTI) tax refund program; and
6. have exhibited a ten percent or greater rate of employment growth in the past two years.

The Office of Tourism, Trade, and Economic Development (OTTED) is authorized to carry out both pilot programs by contract with qualified entities. For the business loan pilot program, the bill sets out the business loan application requirements, the loan administrator requirements, and reporting requirements to the Governor and the Legislature on the progress of the loan program. The business loan pilot program is repealed in 2019. OTTED is granted emergency rulemaking powers to quickly implement the business loan pilot program.

For the technical assistance pilot program, the bill establishes the technical assistance that must be offered to qualifying businesses based on Economic Gardening concepts, bidding requirements to administer the technical assistance pilot program (any contract is limited to $1.5 million), reporting requirements to the Governor and the Legislature, and a program review by the Office of Program Policy and Government Accountability.

The bill does have a fiscal impact but does not appropriate funds to implement either pilot program. However, in the Joint Proclamation, the Legislature made provision for legislation authorizing a pilot program to provide up to $10 million in small business loans to stimulate investment in Florida's economy.

HOUSE PRINCIPLES

Members are encouraged to evaluate proposed legislation in light of the following guiding principles of the House of Representatives

- Balance the state budget.
- Create a legal and regulatory environment that fosters economic growth and job creation.
- Lower the tax burden on families and businesses.
- Reverse or restrain the growth of government.
- Promote public safety.
- Promote educational accountability, excellence, and choice.
- Foster respect for the family and for innocent human life.
- Protect Florida's natural beauty.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. EFFECT OF PROPOSED CHANGES:

Present Situation

Economic Conditions

As the national economy has dramatically slowed, Florida's economy has followed suit. This slowdown has affected all areas of the economy including small business operations. Lending institutions have been pulling back from lending and tightening credit requirements over the past ten months to a year. The New York Times reported in March that small businesses were starting to feel the effects of lenders' credit problems.[1] In May 2008, MSNBC reported that a Federal Reserve survey completed in April 2008 showed that 55% of banks had tightened lending standards on business loans, up from 30% in January 2008.[2] News reports nationally and in Florida have pointed out the difficulties businesses with good credit have had in obtaining loans. In July, it was reported that banks struggling with real estate losses were cutting back on business loans "depriving even healthy companies of money for expansion and hiring."[3] On December 26, the Wall Street Journal reported that "even healthy companies are being choked by the lack of credit lines and bank loans." The paper went on to state that businesses are also being squeezed by reduced consumer spending and customers who are paying their bills late.[4] The Miami Herald recently reported that the "credit crunch means that they (businesses) can't get money to float the bills."

Small businesses use credit to finance such things as start-ups, acquisition or expansion of an existing business; to purchase land or buildings; to cover new construction as well as expansion or conversion of existing facilities; to acquire equipment, machinery, furniture, fixtures, supplies, or materials; for long term working capital including the payment of accounts payable and/or for the purchase of inventory; to refinance existing business indebtedness; for short term working capital needs such as seasonal financing, contract performance, construction financing, export production; and for financing against existing inventory and receivables.

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[1] Elizabeth Olson, "Small Firms Find Credit is Tightening," N.Y. Times March 25, 2008.
[2] Associated Press, "Fed reports tighter lending standards," MSNBC.com, May 5, 2008 (on file with the committee).
[3] Peter S. Goodman, "Worried Banks Sharply Reduce Business Loans," N.Y. Times, July 28, 2008 (on file with the committee).
[4] Simona Covel, "Slump Batters Small Business, Threatening Owners' Dreams," Wall St. J., December 26, 2008 (on file with the committee).

Economic Gardening

Economic gardening is a long-term, economic development strategy designed to grow jobs by encouraging entrepreneurial activity in a community, region, or state. In contrast to traditional "economic hunting" strategies aimed at recruiting businesses from outside the community, economic gardening focuses on the job creation potential of small local businesses that already exist in the community.

The concept of economic gardening was pioneered in 1987 by the City of Littleton, Colorado, during a statewide recession.[5] It is based on research by M.I.T. and Federal Reserve Bank of Kansas City economists which shows that the vast majority of new jobs in a local economy are produced by the community's small local businesses, specifically a small group of high-growth businesses called "gazelles"[6] which are second stage businesses employing between ten and 99 employees. These second stage businesses usually also are privately-held, investment grade businesses that generate between $1 million and $50 million in annual revenue, have exhibited double-digit growth rates, and have been in existence for at least three years.

Economic gardening focuses on three main elements:[7]

- Information: The survival and growth of small businesses depends on access to critical information. Access to free or affordable information and consulting services is thus extremely valuable. Programs can provide access to information on markets, customers, and competitors, such as business databases, GIS (geographic information system), and search engine marketing.
- Infrastructure: This element focuses on building and supporting the development of community assets essential to commerce and overall quality of life. In addition to basic physical infrastructure, this element includes quality of life infrastructure (e.g., parks and open spaces) and intellectual infrastructure that provide educational opportunities to help keep companies competitive.
- Connections: Entrepreneurs benefit significantly from interaction and exchange among business owners and resource providers, such as trade associations, think tanks, and academic institutions. Examples of strategies that improve connectivity include business roundtables, peer-to-peer learning sessions, and mentoring programs.

Since the late 1990s, interest in economic gardening has expanded to become part of economic development plans throughout the country in places like Oakland, California; Santa Fe, New Mexico; Madison, Wisconsin; and the states of Wyoming and Georgia.[8] Communities are attracted to this approach for several reasons. It requires fewer public resources than traditional economic development strategies and keeps those resources in the community by investing in local businesses. It can also assist businesses across industry sectors thereby helping communities develop a more diverse economic base. Moreover, rather than abandoning traditional economic development practices of business recruitment, retention, and expansion, economic gardening provides for a more balanced economic development portfolio. As a result, it allows local communities to capitalize on their unique assets and utilize them for long-term growth.

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[5] City of Littleton, "Business/Industry Affairs" located at http://www.littletongov.org/bia/economicgardening/ last viewed 12/30/08.

[6] Kelly Edmiston, Federal Reserve Bank of Kansas City, "The Role of Small and Large Businesses in Economic Development," located at http://www.kc.frb.org/publicat/ECONREV/PDF/2q07edmi.pdf, last viewed 12/30/08.

[7] Federal Reserve Bank of Atlanta, "Economic Gardening Helps Communities Grow Their Own Jobs," Vol. 18, No. 1, 2008, located at http://www.frbatlanta.org/invoke.cfm?objectid= 4AA2C253-5056-9F12-12D9273D84A914EB&method= display_body last viewed 12/30/08.

[8] Steve Quello and Graham Toft, "Economic Gardening: Next Generation Applications for a Balanced Portfolio Approach to Economic Gardening", U.S. Small Business Admin, Dec. 2006, located at http://sba.gov/advo/research/sbe_06_ch06.pdf last viewed 12/30/08.

Qualified Target Industry (QTI) Tax Refund

Currently, Florida does not offer a direct lending program but does offer a number of business incentives, including the Qualified Target Industry Tax Refund or QTI. The QTI incentive is available for companies that create high wage jobs in targeted high value-added industries. The targeted industries include: aviation/aerospace; clean energy; financial/professional services; homeland security/defense; information technology; life sciences; manufacturing; and emerging technologies. This incentive includes refunds on corporate income, sales, ad valorem, intangible personal property, insurance premium, and certain other taxes. Pre-approved applicants who create jobs in Florida receive tax refunds of $3,000 per net new Florida full-time equivalent job created; $6,000 in an Enterprise Zone or rural county. For businesses paying 150 percent of the average annual wage, add $1,000 per job; for businesses paying 200 percent of the average annual salary, add $2,000 per job. The local community where the company locates contributes 20 percent of the total tax refund. There is a cap of $5 million per single qualified applicant in all years, and no more than 25 percent of the total refund approved may be taken in any single fiscal year. New or expanding businesses in selected targeted industries or corporate headquarters are eligible.[9]

The Governor's Office of Tourism, Trade, and Economic Development reports that there are approximately 36,000 QTI eligible businesses in Florida. Of those businesses, 10,320 have between ten and ninety-nine employees.

State Loan Programs

Several states have developed small business lending programs of various types ranging from partial guarantees to direct lending. Examples of two states' programs are below.

Pennsylvania operates the Small Business First (SBF) loan program which provides low interest loans to promote the growth of small manufacturing, industrial, agriculture enterprises, mining enterprises, export-related business, advanced technology and computer-related services, hotels, motels, restaurants, commercial recyclers, and defense-related companies. The loans may be used for working capital, machinery and equipment purchases and upgrades, and land and building acquisition and construction. The working capital maximum is $100,000 or 50% of total project costs, whichever is less. For other eligible projects the loan maximum is $200,000 or 50% of total project costs, whichever is less. One job must be created or retained for each $25,000 loaned. The loan term is up to three years for working capital, 10 years for machinery and equipment, and up to 15 years for land and building.[10]

The state of Georgia administers the Entrepreneur and Small Business Development (ESBD) Loan Guarantee Program. The ESBD Loan Guarantee Program provides partial guarantees to banks for loans to small businesses that cannot otherwise obtain all of their financing needs. The ESBD Loan Guarantee Program's objective is to fund viable ESBD loans that leverage private investment while creating new or expanding existing businesses that will create employment opportunities for rural Georgia. Loan guarantees to lenders are up to 50% of the original principal amount of the lender's loan, or up to $112,500, whichever is less, with the sub-recipient business providing no less than 10% cash equity in the project. The loan guarantee does not cover outstanding or capitalized interest charges. Lenders provide a 1% loan guarantee fee of the guarantee amount to the OneGeorgia Authority at the loan closing. In addition, OneGeorgia requires an on-going annual fee of 0.5% of the outstanding loan balance.[11]

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[9] Enterprise Florida, "Incentives" located at http://eflorida.com/ContentSubpage.aspx?id=472 last viewed 12/30/08.

[10] State of Pennsylvania, "Small Business First," located at http://www.newpa.com/find-and-apply-for-funding/funding-and-program-finder/funding-detail/index.aspx?progId=33 last viewed 12/30/08.

[11] Chapter 413-6-1, Code of Georgia.

Federal Small Business Loan Programs
The Federal Small Business Administration (SBA) administers several loan programs and one in particular, the 7(a) loan, for working capital expenses. 7(a) loans are only available on a guaranty basis. This means they are provided by lenders who choose to structure their own loans by SBA's requirements and who apply and receive a guaranty from SBA on a portion of this loan. Under the guaranty concept, commercial lenders make and administer the loans.

The business applies to a lender for their financing. The lender decides if they will make the loan internally or if the application has some weaknesses which, in their opinion, will require an SBA guaranty if the loan is to be made. The guaranty which SBA provides is only available to the lender. It assures the lender that in the event the borrower does not repay their obligation and a payment default occurs, the Government will reimburse the lender for its loss, up to the percentage of SBA's guaranty. Under this program, the borrower remains obligated for the full amount due. In order to obtain positive consideration for an SBA supported loan, the applicant must be both eligible and creditworthy.

In order to get a 7(a) loan, the applicant must first be eligible. Repayment ability from the cash flow of the business is a primary consideration in the SBA loan decision process but good character, management capability, collateral, and owner's equity contribution are also important considerations. All owners of 20 percent or more are required to personally guarantee SBA loans.

All applicants must be eligible to be considered for a 7(a) loan. The eligibility requirements are designed to be as broad as possible in order that this lending program can accommodate the most diverse variety of small business financing needs. All businesses that are considered for financing under SBA's 7(a) loan program must meet SBA size standards, be for-profit, not already have the internal resources (business or personal) to provide the financing, and be able to demonstrate repayment. Eligibility factors for all 7(a) loans include size, type of business, use of proceeds, and the availability of funds from other sources. [12]

Effect of proposed changes

The bill creates a two-part Economic Gardening program, one for immediate assistance to businesses and the second a long-term technical assistance program. The first part creates the Economic Gardening Business Loan Pilot Program which is a state-financed, direct loan program for certain categories of businesses to encourage job growth. The second part creates the Economic Gardening Technical Assistance Pilot Program which is a business assistance program based on the Economic Gardening model.

Economic Gardening Business Loan Pilot Program
The bill creates the Economic Gardening Business Loan Pilot Program within the Office of Tourism, Trade, and Economic Development (OTTED). The loan program is focused on businesses desiring to expand jobs in the state. Those include businesses that:

1. are for-profit, privately held, investment grade;
2. employ between ten and 99 employees;
3. have been in existence in the state for at least two years;
4. generate between $1 million and $50 million in annual revenue;
5. qualify for the Qualified Target Industry (QTI) tax refund program; and
6. have exhibited a ten percent or greater rate of employment growth in the past two years.

[12] Small Business Administration, "Basic 7(a) Loan Program" located at http://www.sba.gov/services/financialassistance/sbaloantopics/7a/ last viewed 12/30/08.

The qualifications narrow the types of businesses that may take advantage of the loans to limit the program to businesses that fall within the Economic Gardening model. However, it is likely that there are Florida companies that may wish to expand jobs that do not meet this criteria. Many companies that take advantage of the QTI incentive are C corp businesses that pay the state corporate income tax. A large number of Florida businesses are formed as LLCs, limited partnerships, or sub-chapter S corporations and do not pay corporate income tax and would likely not be eligible.

The loans must be used to finance working capital purchases, employee training, or salaries associated with newly created jobs. Job retention does not qualify under the loan program. The maximum loan amount is $250,000 with no minimum loan amount prescribed. The bill establishes a two percent interest rate and requires that the loan be collateralized with all available corporate assets. In the first year of the loan, only interest is due. The loan is paid off over the remaining term of the loan. If the job creation criterion is not met in the first two years of the loan, the interest rate on the loan is raised to the prime rate plus four percent which will provide an incentive to the business to refinance the loan in the private sector and pay off the loan. It is likely that commercial loans available by that time would have a lower interest rate.

The bill sets out what a business must provide in its application for a loan which includes, among other things, basic information about the business such as its principal place of business in the state; how much the applicant may invest in the business in conjunction with a loan, if at all; the total investment from all sources in the business, if any; the number of net new full-time jobs the applicant will create yearly; how the loan will be collateralized; and why the loan is needed to induce the applicant to create more jobs.

The loan program may be administered by one or more not-for-profit entities under contract with OTTED. There are several non-profit entities that have contracted with OTTED in the past to implement OTTED's business hurricane-disaster loan program that could likely fulfill the program's administrative qualifications. Agreements are for a minimum of four years. An administrative entity may make loans to qualifying businesses through the end of the twenty-fourth month after the effective date of the bill. The entity makes loan approval decisions based upon confirmation of a business' application materials and a determination of which applicants are in the best position to utilize a loan to continue making a successful long-term business commitment to the state. The bill sets out the qualifying criteria for the not-for-profit entities such as having five years of experience lending to small business and having existing partnerships with local or regional economic and business development organizations. A lending entity will receive an origination fee of one percent of the loan amount at closing and a nominal monthly servicing fee. The entity returns principal and interest payments as well as any funds collected from a defaulted borrower to OTTED and also makes a report of loan activity and results to OTTED quarterly. The report describes, among other things, the number and wages of jobs created and the type and location of business activity funded. Any funds not disbursed by OTTED at the end of the twenty-fourth month are returned to General Revenue.

OTTED is granted general rulemaking authority as well as emergency rulemaking authority to expedite the implementation of the loan program. Further, OTTED must make semi-annual reports on the progress of the loan program to the President of the Senate, the Speaker of the House, and the Governor. The bill repeals the loan program in 2019.

Economic Gardening Technical Assistance Pilot Program
The second part of the Economic Gardening strategy in the bill provides authority to OTTED to contract, after competitive bidding, with an entity to implement the Economic Gardening Technical Assistance Pilot Program based on the Economic Gardening model described in the Present Situation section above. Passage of the bill would begin the process of moving into Economic Gardening, which is a new economic development strategy for the state. The bill provides that the program will focus on

providing technical and counseling assistance to the same type of businesses that qualify for the loan program which includes businesses that:

1. are for-profit, privately held, investment grade;
2. employ between ten and 99 employees;
3. have been in existence in the state for at least two years;
4. generate between $1 million and $50 million in annual revenue;
5. qualify for the Qualified Target Industry (QTI) tax refund program; and
6. have exhibited a ten percent or greater rate of employment growth in the past two years.

The entity must demonstrate to OTTED its ability to implement an economic gardening program with a emphasis on the third party's capability to provide, on a statewide basis, counseling services, access to technology and information, marketing services and advice, business management support, and other similar services. The contract amount may not exceed $1.5 million. Once a contract is awarded, the bill specifies that the entity must choose businesses in various industry categories and attempt to assist businesses throughout the state. A business receiving assistance must enter into an agreement with the entity that it will meet with the entity on a regular basis and provide the necessary business information for the entity to track the progress of the business and the effectiveness of the assistance provided. The entity must report the information collected to OTTED on a quarterly basis. The bill provides that the entity is an economic development organization as defined in s. 288.075, F.S., authorized to promote the general business interests or industrial interests of the state. OTTED must semi-annually review the entity to insure the contract parameters are being met. If the contract is not being fulfilled, OTTED may terminate and re-bid.

The bill requires OTTED to provide an annual report to the President of the Senate, the Speaker of the House, and the Governor detailing the progress of the Economic Gardening technical assistance pilot program. OTTED is also provided rulemaking authority to implement the program.
Three years from the effective date of the act, the bill requires the Office of Program Policy Analysis and Government Accountability (OPPAGA) to conduct a review of the Economic Gardening technical assistance pilot program and its effectiveness in growing the targeted businesses and OPPAGA must provide a report to the President of the Senate, the Speaker of the House of Representatives, and the Governor.

The bill takes effect upon becoming law.

B. SECTION DIRECTORY:

Section 1: creates the Economic Gardening Business Loan Pilot Program.

Section 2: creates the Economic Gardening Technical Assistance Pilot Program.

Section 3: provides for a program review of the Economic Gardening Technical Assistance Pilot Program.

Section 4: provides a limit of $1.5 million on the amount of the contract for implementation of the Economic Gardening Technical Assistance Pilot Program.

Section 5: provides an effective date.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

   The bill may generate a nominal return to General Revenue from the two-percent interest rate charged in the Economic Gardening Business Loan Pilot Program.

2. Expenditures:

   The bill does not make an appropriation to fund the Economic Gardening Business Loan Pilot Program nor the Economic Gardening Technical Assistance Pilot Program. However, in the Joint Proclamation issued on December 30, 2008, the Legislature made provision for legislation authorizing a pilot program to provide up to $10 million in small business loans to stimulate investment in Florida's economy.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

   None.

2. Expenditures:

   None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

The bill provides for a state-funded, direct loan program that could provide loans up to $250,000 which, for certain qualified businesses, could help those businesses create jobs. However, state-funded, direct loans may reduce the number of private sector loans that may be made and could have an indeterminate impact on commercial lending institutions, although it has been reported that commercial loans have become more difficult to obtain. The technical assistance portion of the bill could help businesses grow and expand which, in the long term, could help diversify the state's economy.

D. FISCAL COMMENTS:

None.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

   Not applicable. This bill does not appear to affect county or municipal government.

2. Other:

Article VII, section 10 of the state constitution prohibits the state, any local government, or their agents from becoming a joint owner with, or stockholder of, or from giving, lending or using its taxing power or credit to aid any corporation, association, partnership or person.[13] The supreme court recently restated its interpretation of this constitutional prohibition, construing the restriction related to the lending of credit to "not just the use of public funds but the imposition of a new financial liability and a direct or indirect obligation to pay a debt of a third party."[14] The bill's provisions regarding the business loan pilot program only lends money to a business to use for working capital purchases that must create jobs and does not obligate the state in any way to the debts of the borrower owed to the borrower's creditors. It appears that the business loan pilot program would not violate the constitutional provision described based on the court's narrow interpretation of this provision.

B. RULE-MAKING AUTHORITY:

The Office of Tourism, Trade, and Economic Development (OTTED) is granted rulemaking power to implement both the Economic Gardening Business Loan Pilot Program and the Economic Gardening Technical Assistance Pilot Program. Further, OTTED is granted emergency rulemaking power to expedite the implementation of the Economic Gardening Business Loan Pilot Program.

C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

IV. AMENDMENTS/COUNCIL OR COMMITTEE SUBSTITUTE CHANGES

N/A

[13] Art. VII, Section 10, Fla. Const. Pledging credit.— Neither the state nor any county, school district, municipality, special district, or agency of any of them, shall become a joint owner with, or stockholder of, or give, lend or use its taxing power or credit to aid any corporation, association, partnership or person; but this shall not prohibit laws authorizing:
(a) the investment of public trust funds;
(b) the investment of other public funds in obligations of, or insured by, the United States or any of its instrumentalities;
(c) the issuance and sale by any county, municipality, special district or other local governmental body of (1) revenue bonds to finance or refinance the cost of capital projects for airports or port facilities, or (2) revenue bonds to finance or refinance the cost of capital projects for industrial or manufacturing plants to the extent that the interest thereon is exempt from income taxes under the then existing laws of the United States, when, in either case, the revenue bonds are payable solely from revenue derived from the sale, operation or leasing of the projects. If any project so financed, or any part thereof, is occupied or operated by any private corporation, association, partnership or person pursuant to contract or lease with the issuing body, the property interest created by such contract or lease shall be subject to taxation to the same extent as other privately owned property.
(d) a municipality, county, special district, or agency of any of them, being a joint owner of, giving, or lending or using its taxing power or credit for the joint ownership, construction and operation of electrical energy generating or transmission facilities with any corporation, association, partnership or person.

[14] *Jackson-Shaw Company v. Jacksonville Aviation Authority,* 2008 WL 5245640, p. 19 (Fla.) Dec. 18, 2008.